



Newfoundland and Labrador Government Sinking Fund

Government of Newfoundland and Labrador
Department of Finance

Annual Report

31 March, 2007

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**BOARD OF TRUSTEES
NEWFOUNDLAND AND LABRADOR CONSOLIDATED SINKING FUNDS**

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
NEWFOUNDLAND AND LABRADOR MUNICIPAL FINANCING
CORPORATION SINKING FUND

DEBT MANAGEMENT DIVISION
DEPARTMENT OF FINANCE
CONFEDERATION BUILDING
P. O. BOX 8700
ST. JOHN'S, NL
A1B 4J6

February 25, 2008

Honourable Thomas W. Marshall, QC
Minister of Finance
Government of Newfoundland and Labrador
Confederation Building
St. John's, NL
A1B 4J6

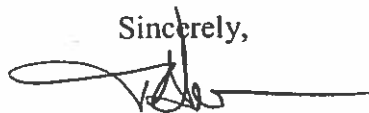
Dear Minister Marshall:

I am pleased to present the Annual Activity Report for the Board of Trustees of the Newfoundland and Labrador Government Sinking Fund. This Report summarizes activities for the fiscal year ended March 31, 2007.

The Newfoundland and Labrador Government Sinking Fund administers the sinking funds established for the repayment of the Province's debenture debt. The effective management of these trustee funds contributes to the Department of Finance's responsibilities with respect to stewardship of public money and strong fiscal management.

This Report was prepared under the direction of the Board of Trustees and the Board is accountable for the results reported herein.

Sincerely,



Terry Paddon
Chairman

**Newfoundland and Labrador
Government Sinking Fund**

**Activity Report
March 31, 2007**

Overview

The Newfoundland and Labrador Government Sinking Fund was created pursuant to the *Financial Administration Act* to consolidate and administer sinking funds established for the repayment of the Province's debenture debt. The Province has established sinking funds for most of its long term debenture issues and the annual contributions to these sinking funds are invested by the Board of Trustees of the Newfoundland and Labrador Consolidated Sinking Funds, appointed by the Lieutenant Governor in Council to manage and control the day to day operation of the sinking funds.

The Board consists of the incumbents in five senior public service positions with the Department of Finance. At 31 March 2007 the Board included:

Mr. Terry Paddon (Chair)
Deputy Minister

Mr. Ron Williams
Comptroller General

Ms. Donna Brewer
Assistant Deputy Minister
Financial Planning and Benefits Administration

Mr. Earl Saunders
Director of Debt Management

Ms. Linda Howell
(Trustee and Secretary)
Manager of Debt Servicing and Financial Risk

Mandate

The mandate of the Board of Trustees is to manage and control the operational activities of the Newfoundland and Labrador Government Sinking Fund and the sinking funds of certain Crown corporations where the Province has guaranteed the related debt (i.e. Newfoundland and Labrador Municipal Financing Corporation and the Eastern Regional Integrated Health Authority). These activities include setting investment policy, investment of trusteed funds and the monitoring of such. These trusteed funds are invested in accordance with the *Financial Administration Act*, primarily in bonds, debentures or other securities issued or guaranteed by the Government of Canada, the government of a province of Canada, or a chartered bank, with the goal of earning the maximum return from investment of the portfolio while ensuring security of the funds.

Sources of Funding

For debenture issues which have sinking fund requirements, the Province makes the required sinking fund payments to the Board of Trustees. In 2006-07 these sinking fund payments amounted to some \$44 million. The sinking fund contributions are invested and the interest earnings, less an amount to cover administrative costs, are re-invested.

Highlights and Accomplishments

A net income of \$56.3 million was earned by the Sinking Fund during 2006-07. This consisted of \$56.5 million in revenues, less \$0.2 million for salaries and general administrative expenses. Four operational staff, employees of the Department of Finance, perform duties on behalf of the Sinking Fund, as well as the Department. The Sinking Fund pays a portion of the salary of these employees.

Activities

- For the fiscal year ended March 31, 2007 sinking fund assets of \$946 million were invested within applicable legislative parameters and the approved investment strategy of the Board of Trustees.
- During 2006-07, longer term investments of \$43 million were purchased for the Sinking Fund, using funds provided from the operating income and statutory contributions made by the Province. The remainder of funds was invested short-term, with a minimal amount retained as cash in a bank account.

Opportunities and Challenges

During the upcoming fiscal year, the Newfoundland and Labrador Government Sinking Fund will complete a review of its current investment strategy, with a view to determining if returns can be enhanced while continuing to ensure security of the funds. If necessary, changes to legislation will be recommended to allow for an enhanced return on invested sinking fund assets.

Financial Statements

The audited financial statements of the Sinking Fund for the year ended March 31, 2007 are attached. These financial statements have not been, and were not intended to be, prepared in accordance with Canadian generally accepted accounting principles with respect to the impact of foreign currency translation adjustments resulting from the translation of U.S. dollar denominated investments. Since the policy of the Newfoundland and Labrador Government Sinking Fund is to hold its U.S. dollar investments to maturity and never convert them to Canadian dollars, gains and losses arising from fluctuations of the currency are unrealized and are shown as a separate component of the Sinking Fund Equity, rather than as realized gains and losses shown on the Statement of Revenue and Expenditure.

**NEWFOUNDLAND AND LABRADOR
GOVERNMENT SINKING FUND**

FINANCIAL STATEMENTS

31 MARCH 2007



OFFICE OF THE AUDITOR GENERAL
St. John's, Newfoundland and Labrador

AUDITOR'S REPORT

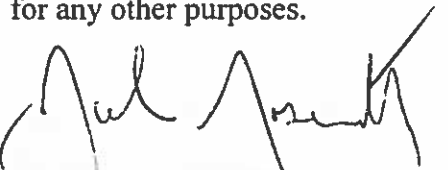
To the Board of Trustees
Newfoundland and Labrador Government Sinking Fund
St. John's, Newfoundland and Labrador

I have audited the balance sheet of the Newfoundland and Labrador Government Sinking Fund as at 31 March 2007 and the statements of statutory contributions, retained earnings, revenues and expenses, and cash flows for the year then ended. These financial statements have been prepared to meet the information needs of the Board of Trustees and the Government of Newfoundland and Labrador under Section 39 of the *Financial Administration Act* and under the various debentures which require the establishment of sinking funds. These financial statements are the responsibility of the Board's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at 31 March 2007 and the results of its operations and its cash flows for the year then ended in accordance with the basis of accounting described in Note 1 to the financial statements.

These financial statements, which have not been, and were not intended to be, prepared in accordance with Canadian generally accepted accounting principles, are solely for the information and use of the Board of Trustees of the Newfoundland and Labrador Government Sinking Fund and the Government of Newfoundland and Labrador to meet their information needs under Section 39 of the *Financial Administration Act* and under the various debentures which require the establishment of sinking funds. The financial statements are not intended to be and should not be used by anyone other than the specified users or for any other purposes.


JOHN L. NOSEWORTHY, CA
Auditor General

St. John's, Newfoundland and Labrador
20 June 2007

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
INDEX TO FINANCIAL STATEMENTS
31 March 2007

Balance Sheet	Statement 1
Statement of Statutory Contributions	” 2
Statement of Retained Earnings	” 3
Statement of Revenues and Expenses	” 4
Statement of Cash Flows	” 5
Schedule of Investments	Schedule 1

**NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
BALANCE SHEET**

31 March	2007	2006
	(000's)	(000's)
ASSETS		
Current		
Cash	\$ 90	\$ 69
Term deposits and short-term investments, at cost	65,931	12,185
Interest and other receivables		
Province of Newfoundland and Labrador – guaranteed	11,459	10,936
Other	3,797	3,665
	<u>81,277</u>	<u>26,855</u>
Investments, at amortized cost (Schedule 1)		
Cost	772,483	739,689
Accumulated amortization of discounts and premiums	92,678	82,560
	<u>865,161</u>	<u>822,249</u>
	<u>\$ 946,438</u>	<u>\$ 849,104</u>
LIABILITIES AND SINKING FUND EQUITY		
Current		
Accounts payable and accrued liabilities	\$ 12	\$ 12
Due to Province of Newfoundland and Labrador	14	12
	<u>26</u>	<u>24</u>
Sinking fund equity		
Statutory contributions (Statement 2)	496,829	454,350
Retained earnings (Statement 3)	449,583	394,730
	<u>946,412</u>	<u>849,080</u>
	<u>\$ 946,438</u>	<u>\$ 849,104</u>

See accompanying notes

Signed on behalf of the Board:


Chairperson


Member

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND**STATEMENT OF STATUTORY CONTRIBUTIONS****For the Year Ended 31 March**

	2007	2006
	(000's)	(000's)
Balance, beginning of year	\$ 454,350	\$ 415,296
Statutory contributions for the year	44,348	44,472
	498,698	459,768
Foreign currency translation adjustment	(1,869)	(5,418)
Balance, end of year	\$ 496,829	\$ 454,350

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
STATEMENT OF RETAINED EARNINGS
For the Year Ended 31 March

	2007	2006
	(000's)	(000's)
Balance, beginning of year	\$ 394,730	\$ 347,316
Excess of revenues over expenses	56,259	52,373
	450,989	399,689
Foreign currency translation adjustment	(1,406)	(4,959)
Balance, end of year	\$ 449,583	\$ 394,730

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND**STATEMENT OF REVENUES AND EXPENSES****For the Year Ended 31 March**

	2007	2006
	(000's)	(000's)
REVENUES		
Interest income		
Debentures	\$ 45,209	\$ 41,558
Term deposits and short-term investments	1,541	1,227
Other	17	16
	<u>46,767</u>	<u>42,801</u>
<u>Amortization of discounts and premiums</u>	<u>9,734</u>	<u>9,889</u>
	<u>56,501</u>	<u>52,690</u>
EXPENSES		
Salaries and benefits	125	200
<u>General</u>	<u>117</u>	<u>117</u>
	<u>242</u>	<u>317</u>
<u>Excess of revenues over expenses</u>	<u>\$ 56,259</u>	<u>\$ 52,373</u>

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND**STATEMENT OF CASH FLOWS****For the Year Ended 31 March**

	2007	2006
	(000's)	(000's)
Cash flows from operating activities		
Excess of revenues over expenses	\$ 56,259	\$ 52,373
Adjustment for non-cash item		
<u>Amortization of discounts and premiums</u>	<u>(9,734)</u>	<u>(9,889)</u>
	46,525	42,484
<u>Change in non-cash working capital</u>	<u>(653)</u>	<u>(1,875)</u>
	<u>45,872</u>	<u>40,609</u>
Cash flows from financing activities		
Statutory contributions	44,348	44,472
Effect of foreign currency on statutory contributions	(1,869)	(5,418)
<u>Effect of foreign currency on retained earnings</u>	<u>(1,406)</u>	<u>(4,959)</u>
	41,073	34,095
Cash flows from investing activities		
Purchase of investments	(43,210)	(122,323)
Proceeds from redemption and sale of investments	6,549	5,256
<u>Effect of foreign currency on investments</u>	<u>3,483</u>	<u>8,681</u>
	<u>(33,178)</u>	<u>(108,386)</u>
Net increase (decrease) in cash and cash equivalents	53,767	(33,682)
Cash and cash equivalents, beginning of year	12,254	45,936
Cash and cash equivalents, end of year	\$ 66,021	\$ 12,254
Cash and cash equivalents include:		
Cash	\$ 90	\$ 69
<u>Term deposits and short-term investments</u>	<u>65,931</u>	<u>12,185</u>
	<u>\$ 66,021</u>	<u>\$ 12,254</u>

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND

SCHEDULE OF INVESTMENTS

31 March

2007

2006

	<u>Face Value or Par</u> (000's)	<u>Amortized Cost</u> (000's)	<u>Face Value or Par</u> (000's)	<u>Amortized Cost</u> (000's)
Canadian				
Province of Newfoundland and Labrador - guaranteed				
Province of Newfoundland and Labrador	\$ 186,946	\$ 196,964	\$ 180,870	\$ 190,526
Newfoundland and Labrador Municipal Financing Corporation	50,773	50,787	53,073	53,106
Coupons and residuals	324,612	181,204	319,123	167,231
	562,331	428,955	553,066	410,863
Other securities	83,087	85,302	70,087	72,939
Other coupons and residuals	58,567	40,863	57,804	38,202
	703,985	555,120	680,957	522,004
U.S.				
Province of Newfoundland and Labrador - guaranteed				
Province of Newfoundland and Labrador	155,534	176,411	143,926	162,114
Other securities	114,767	124,271	118,435	129,324
Other coupons and residuals	17,512	9,359	17,715	8,807
	287,813	310,041	280,076	300,245
Total investments	\$ 991,798	\$ 865,161	\$ 961,033	\$ 822,249

See accompanying notes

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
NOTES TO FINANCIAL STATEMENTS
31 March 2007

Authority

The Province of Newfoundland and Labrador issues debentures, most of which have sinking fund requirements. For debentures which have sinking fund requirements, the Province makes the required sinking fund payments (statutory contributions) to the Board of Trustees of the Newfoundland and Labrador Government Sinking Fund. This is an unincorporated body formed under the *Financial Administration Act*. All members of the Board are full-time employees of the Province and are appointed by the Lieutenant-Governor in Council.

1. Basis of accounting

These financial statements have been prepared by the Board's management in accordance with the significant accounting policies set out below to meet the information needs of the Board of Trustees of the Newfoundland and Labrador Government Sinking Fund and the Government of Newfoundland and Labrador under Section 39 of the *Financial Administration Act* and under the various debentures which require the establishment of sinking funds. The basis of accounting used in these financial statements materially differs from Canadian generally accepted accounting principles because the impact of foreign currency translation adjustments arising from the translation of U.S. denominated investments is not recognized in income during the year. These gains or losses are unrealized and it is intended that they will remain so since it is not the intention of the Fund that these investments, which are held in U.S. funds, will ever actually be converted to Canadian dollars.

(a) Cash and cash equivalents

Cash and cash equivalents include balances with banks, and term deposits and short-term investments with original maturities of three months or less.

(b) Investment transactions

- (i) Purchases: Investments are initially recorded at cost.
- (ii) Amortization: Discounts and premiums are amortized on a straight-line basis from the date of purchase until maturity.
- (iii) Sales: Sales of investments are at a negotiated selling price. Sales are recorded at the proceeds less the investment's average amortized cost, with any resulting gain or loss also recorded.
- (iv) Redemptions: On occasion, investments held in the Fund will be called for redemption by the issuer. In such instances, a gain is recorded equal to the redemption proceeds less the investment's average amortized cost.

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
NOTES TO FINANCIAL STATEMENTS
31 March 2007

1. Basis of accounting (cont.)

- (c) Maturity of a Province of Newfoundland and Labrador debenture issue for which a sinking fund has been provided.

(i) General

Provision is made for redemption at debenture maturity by investing statutory contributions in interest bearing securities and other investments. Both the contributions and the interest are used to pay debenture holders when debentures mature.

A record is maintained of statutory contributions received on account of each issue and of income allocated to each issue (retained earnings). The dollar total of an issue's statutory contributions and allocated income is called its Sinking Fund Value.

At maturity, statutory contributions are reduced by the total amount of statutory contributions received over the life of the issue. Retained earnings are reduced by the excess of the debenture's Sinking Fund Value over statutory contributions received.

(ii) Cash flow

At maturity, cash is paid into a redemption bank account in an amount equal to the lesser of the total face value of the issue or the Sinking Fund Value of the issue, less the face value of the issue held in the Fund's investments. If the issue's Sinking Fund Value exceeds the total face value, the excess is paid to the Consolidated Revenue Fund of the Province of Newfoundland and Labrador. If the issue's Sinking Fund Value is less than the total face value, the difference is paid into the redemption bank account by the Province.

- (d) Interest income

Interest income is recorded on an accrual basis.

- (e) Foreign currency translation

Assets, liabilities, revenues and expenses denominated in U.S. currency are translated as follows:

- (i) assets and liabilities are translated at the rate of exchange in effect at the balance sheet date; and
(ii) revenues and expenses are translated at the rate of exchange in effect on the dates on which such items are recognized in income during the year, or an average of such.

Foreign currency translation adjustments arising from the translation of U.S. denominated investments are deferred and shown as separate components of the sinking fund equity. These gains or losses are unrealized and it is intended that they will remain so since it is not the intention of the Fund that these investments, which are held in U.S. funds, will ever actually be converted to Canadian dollars.

NEWFOUNDLAND AND LABRADOR GOVERNMENT SINKING FUND
NOTES TO FINANCIAL STATEMENTS
31 March 2007

2. Related party transactions

The Newfoundland and Labrador Government Sinking Fund and the Province absorb all of the operating costs, with the exception of banking and custodial fees, of the Newfoundland and Labrador Municipal Financing Corporation Sinking Fund, which is administered by the same Board as the Newfoundland and Labrador Government Sinking Fund.

3. Financial instruments

The Newfoundland and Labrador Government Sinking Fund's short-term financial instruments recognized on the balance sheet consist of cash, term deposits and short-term investments, interest and other receivables, accounts payable and accrued liabilities and due to Province of Newfoundland and Labrador. The carrying values of these instruments approximate current fair value due to their nature and the short-term maturity associated with them.

The Fund holds long-term investments which have an amortized cost of \$865,161,000 (2006 - \$822,249,000). The face value of these investments is \$991,798,000 (2006 - \$961,033,000). The policy and intention of the Board is to hold these long-term investments to maturity. Therefore, their reported value is current fair value to the Fund and there is no rate risk associated with these investments.

4. Income taxes

The Newfoundland and Labrador Government Sinking Fund is a Crown entity of the Province of Newfoundland and Labrador and as such is not subject to Provincial or Federal income taxes.